

# Indian Hotels Company

5 September 2019

Reuters: IHTL.NS; Bloomberg: IH IN

## Cost optimization - driver of profitability

We recently met the management of Indian Hotels Company Limited (IHCL). Management indicated that it is focusing on a four pronged strategy for earnings growth. The key drivers of the profit growth are expected to be: (1) RevPar growth (2) Cost optimization (3) Growth in Food and Beverages (F&B) (4) Increase in memberships of club 'Chambers' and (5) Increase in management contracts. RevPar and F&B growth YTD has been relatively muted due to slower growth from MICE and corporate segments.

Management stated that growth for 2QFY20 till date has been muted relative to expectations due to: (1) Flat RevPar in July 2019 and slow RevPar growth in August 2019 (2) Continued underperformance by Corporate and MICE segments (3) Flat occupancies; marginal reduction in ARR (4) International operations (UK) performing better due to sports events.

While the RevPar and F&B growth YTD FY20E has been muted, management is hopeful that 2HFY20 will grow at a stronger pace. Historically, second half of the year has contributed to 70% of the full year profits.

Post our discussion with management and with other industry experts, we have revised our estimates for IHCL. Post revision, EBITDA is expected to grow at a three year CAGR (FY19 – FY22E) of 10% to Rs11,118mn in FY22E.

We have retained our Buy rating on the stock with a revised target price (TP) of Rs168 (Rs206 earlier). We have rolled over from FY21E to midpoint FY22E and valued the company at 21x mid year FY22E EV/EBITDA. The downward revision of TP is attributable to downward revision of RevPar estimates.

**Revenue to be impacted because of muted RevPar and F&B:** Weakness in Corporate and MICE segments till date is expected to maintain pressure on RevPar in 2QFY20E. Although the RevPar is expected to post a YoY growth in 2QFY20E, growth would be lower than earlier expectations. The company expects to maintain the occupancy level but ARR is expected to trend marginally lower. Because of the slow growth of Corporate and MICE segments, the F&B segment is also expected to post lower revenue. However, revenue growth is expected to be supported by increase in management contracts and increase in membership of 'Chambers'

**EBITDA to be driven by cost optimization:** EBITDA is expected to grow at a three year CAGR (FY19 – FY22E) of 10% to Rs11,118mn in FY22E; Revenue CAGR during the three year (FY19-22E) is expected to be 7%. This is driven by cost optimization measures undertaken by management. Some of the measures undertaken include: (1) Utilities - A joint venture with Tata Power Company for solar energy and also working with Siemens to take measures for reducing energy consumption. (2) Manpower - While the company plans to maintain its manpower-to-room ratio at 1.9:1, it expects the costs to gradually reduce with the retirement of high-cost senior employees and also hiring of relatively low-cost employees (3) Cluster-based shared services like common accounting, finance etc, (4) Synergies to be created by merging of the sales force of Taj and Ginger hotels. (5) Standardisation of equipment to get the benefits of discount through bulk buying of items like glasses, chairs etc.

**Capex of Rs4,500mn in FY20:** Management indicated that capex of Rs4.5bn for FY20E is expected to be driven by capex for Ginger, Santacruz, Taj Mansingh, SeleQtions Connaught, Holiday Village, maintenance activities and other hotels.

**Gross debt to marginally decline during FY20:** Management has indicated that the gross debt is not expected to increase in FY20E. Most of the capex is expected to be supported by cash flows generated from non core asset sale.

**Monetization of non-core assets on track:** Management strategy to monetize non-core assets is on track. Management informed that it has monetized non-core assets worth Rs750mn during the year and is hopeful of sales of Rs2.5bn for FY20E.

**Maintain Buy with revised TP of Rs168 (earlier Rs206):** We have rolled over our valuation from FY21E to midpoint FY22E. Our revised TP of Rs168 (earlier Rs206) for IHCL is based on 21x mid year FY22E EV/EBITDA, which is supported by EBITDA CAGR of 10% over FY19-FY22E. The muted growth YTD FY20 in RevPar has led to our reduction in RevPar growth from 8% annually (FY20-22E) to 5%-6% annually (FY20-22E). However, we maintain that the hotel sector is in a cyclical upswing with improvement in RevPar albeit lower than expected, and also increase in the number of rooms driving higher revenue. Higher revenue, together with a relatively muted rise in costs and high operational leverage are expected to lead to strong growth in EBITDA. Our optimism is further supported by a healthy balance sheet and negative working capital.

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Revenues	41,036	45,119	48,083	51,266	55,482
YoY (%)	2.3	10.0	6.6	6.6	8.2
EBITDA	6,703	8,297	8,938	10,119	11,118
EBITDA Margin (%)	16.3	18.4	18.6	19.7	20.0
PAT	632	2,445	2,913	3,867	4,631
YoY (%)	NA	287	19.1	32.8	19.7
Adjusted PAT	1,009	2,868	3,337	4,281	5,042
YoY (%)	NA	184.3	16.4	28.3	17.8
EPS (Rs)*	0.85	2.41	2.81	3.60	4.24
RoE (%)	2.4	6.6	7.1	8.4	9.0
EV/EBITDA (x)	27.7	20.0	18.2	16.2	14.1
P/E (x)	179.0	63.0	47.2	36.8	31.3

Source: Company, Nirmal Bang Institutional Equities Research

\*Note: EPS is calculated on Adjusted PAT

## BUY

Sector: Hotel

CMP: Rs133

Target Price: Rs168

Upside: 26%

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### Key Data

Current Shares O/S (mn)	1,189.3
Mkt Cap (Rsbn/US\$bn)	158.2/2.2
52 Wk H / L (Rs)	164/109
Daily Vol. (3M NSE Avg.)	940,060

### Price Performance (%)

	1 M	6 M	1 Yr
Indian Hotels	(1.8)	(4.3)	3.5
Nifty Index	(0.2)	(1.3)	(5.5)

Source: Bloomberg

## Impact of Changes

Particulars	FY20E	FY21E	FY22E
<b>RevPar (Rs)</b>			
Earlier	4,332	4,679	5,053
Growth (%)	8%	8%	8%
Revised	4,212	4,465	4,688
Growth (%)	5%	6%	5%
<b>EBDITA (Rs mn)</b>			
Earlier	10,437	12,699	15,423
Revised	8,938	10,119	11,118
<b>EBDITA Margins (%)</b>			
Earlier	21.1%	23.6%	25.7%
Revised	18.6%	19.7%	20.0%
<b>Net Debt (Rs mn)</b>			
Earlier	18,664	13,198	6,492
Revised	18,997	14,589	10,080
<b>Operating Cashflows (Rs mn)</b>			
Earlier	8,439	10,529	12,144
Revised	7,561	8,977	9,582
<b>EPS (Rs)</b>			
Earlier	3.63	5.05	6.71
Revised	2.81	3.60	4.24
<b>Net Asset Value (Rs mn)</b>			
Earlier		2,45,492	
Revised		1,99,176	

Source: Company, Nirmal Bang Institutional Equities Research

## Financial statement

### Exhibit 1: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
<b>Net sales</b>	<b>41,036</b>	<b>45,120</b>	<b>48,083</b>	<b>51,266</b>	<b>55,482</b>
Growth YoY (%)	2.3	10.0	6.6	6.6	8.2
COGS	3,764	4,041	4,508	4,778	5,152
Operating costs	16,057	14,708	18,431	19,353	20,866
Other expenses	14,510	18,074	16,207	17,017	18,348
<b>EBITDA</b>	<b>6,703</b>	<b>8,297</b>	<b>8,938</b>	<b>10,119</b>	<b>11,118</b>
<b>EBITDA growth (%)</b>	<b>10.0</b>	<b>23.8</b>	<b>7.7</b>	<b>13.2</b>	<b>9.9</b>
<b>EBITDA margin (%)</b>	<b>16.3</b>	<b>18.4</b>	<b>18.6</b>	<b>19.7</b>	<b>20.0</b>
Depreciation	3,012	3,279	3,733	3,893	4,158
<b>EBIT</b>	<b>3,691</b>	<b>5,019</b>	<b>5,205</b>	<b>6,225</b>	<b>6,959</b>
<b>EBIT (%)</b>	<b>9.0</b>	<b>11.1</b>	<b>10.8</b>	<b>12.1</b>	<b>12.5</b>
Interest expense	2,690	1,901	1,733	1,373	1,013
Other income	617	834	875	919	965
Others	225	66	-	-	-
<b>Earnings before tax</b>	<b>1,843</b>	<b>4,017</b>	<b>4,347</b>	<b>5,772</b>	<b>6,912</b>
Tax- total	1,211	1,571	1,435	1,905	2,281
Rate of tax (%)	65.7	39.1	33.0	33.0	33.0
<b>Net profit</b>	<b>632</b>	<b>2,446</b>	<b>2,913</b>	<b>3,867</b>	<b>4,631</b>
<b>Adjusted PAT</b>	<b>1,009</b>	<b>2,868</b>	<b>3,337</b>	<b>4,281</b>	<b>5,042</b>
% growth	N/A	184.3	16.4	28.3	17.8
EPS (FD)	0.85	2.41	2.81	3.60	4.24
% growth	N/A	184.3	16.4	28.3	17.8

\* Adjusted PAT - After minority interest and Share of associates and JV

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 3: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Share capital	1,189	1,189	1,189	1,189	1,189
Reserves and surplus	40,622	42,291	45,628	49,909	54,951
<b>Net worth</b>	<b>41,812</b>	<b>43,480</b>	<b>46,818</b>	<b>51,098</b>	<b>56,140</b>
Loans	24,274	23,260	21,660	17,160	12,660
Minority interest	7,774	7,999	7,999	7,999	7,999
Provision	836	1,023	1,074	1,128	1,185
Deferred tax liability	3,563	3,768	3,956	4,154	4,362
Other non-current liability	2,536	1,798	1,735	1,822	1,913
<b>Total capital employed</b>	<b>80,794</b>	<b>81,328</b>	<b>83,242</b>	<b>83,361</b>	<b>84,258</b>
Goodwill on consolidation	5,655	5,835	5,835	5,835	5,835
Property, plant and equipment	57,941	59,550	60,318	60,324	60,966
Investments	11,809	11,239	11,239	11,239	11,239
Loans	151	157	157	157	157
Other non-current assets	5,994	7,469	7,842	8,234	8,646
<b>Total non-current assets</b>	<b>81,550</b>	<b>84,250</b>	<b>85,391</b>	<b>85,790</b>	<b>86,843</b>
Trade payables	3,513	3,253	3,539	3,731	3,990
Other current liabilities	8,055	9,696	10,183	10,692	11,227
Provisions (current)	1,384	1,476	1,550	1,628	1,709
<b>Total current liabilities</b>	<b>12,952</b>	<b>14,425</b>	<b>15,272</b>	<b>16,051</b>	<b>16,926</b>
Inventories	857	804	1,180	1,244	1,330
Investments	3,305	2,112	2,218	2,329	2,445
Trade receivables	3,286	3,214	3,952	4,214	4,560
Cash and bank balance	2,703	2,409	2,663	2,571	2,579
Loans and advances	91	34	34	34	34
Other current assets	1,953	2,930	3,076	3,230	3,392
<b>Total current assets</b>	<b>12,195</b>	<b>11,504</b>	<b>13,123</b>	<b>13,622</b>	<b>14,340</b>
<b>Net current assets</b>	<b>(757)</b>	<b>(2,922)</b>	<b>(2,149)</b>	<b>(2,429)</b>	<b>(2,585)</b>
<b>Total capital employed</b>	<b>80,794</b>	<b>81,328</b>	<b>83,242</b>	<b>83,361</b>	<b>84,258</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 2: Cash flow

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
<b>PAT after MI &amp; share in associates &amp; JV</b>	<b>1,009</b>	<b>2,868</b>	<b>3,337</b>	<b>4,281</b>	<b>5,042</b>
Depreciation	3,012	3,279	3,733	3,893	4,158
Finance costs	2,690	1,901	1,733	1,373	1,013
Other income	617	834	875	919	965
Working capital changes	(2,080)	1,998	(367)	350	334
<b>Operating cash flow</b>	<b>4,014</b>	<b>9,211</b>	<b>7,561</b>	<b>8,977</b>	<b>9,582</b>
Capital expenditure	(6,115)	(4,901)	(4,500)	(3,900)	(4,800)
<b>Net cash after capex</b>	<b>(2,102)</b>	<b>4,310</b>	<b>3,061</b>	<b>5,077</b>	<b>4,782</b>
Other income/(expense)	(389)	15	537	564	592
Issue/(buyback of equity)	14,914	(0)	-	-	-
Proceeds/repayment of borrowings	(9,556)	(1,015)	(1,600)	(4,500)	(4,500)
Finance costs	(2,690)	(1,901)	(1,733)	(1,373)	(1,013)
Others	(74)	(1,720)	134	140	148
<b>Cash flow from financing</b>	<b>2,595</b>	<b>(4,636)</b>	<b>(3,199)</b>	<b>(5,732)</b>	<b>(5,365)</b>
<b>Total cash generation</b>	<b>105</b>	<b>(311)</b>	<b>399</b>	<b>(92)</b>	<b>8</b>
Opening cash balance	2,471	2,703	2,409	2,663	2,571
<b>Closing cash &amp; bank balance</b>	<b>2,703</b>	<b>2,409</b>	<b>2,663</b>	<b>2,571</b>	<b>2,579</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 4: Key ratios

Y/E March	FY18	FY19	FY20E	FY21E	FY22E
<b>Profitability and return ratios</b>					
EBITDA margin (%)	16.3	18.4	18.6	19.7	20.0
EBIT margin (%)	9.0	11.1	10.8	12.1	12.5
Net profit margin (%)	2.5	6.4	6.9	8.3	9.1
RoE (%)	2.4	6.6	7.1	8.4	9.0
RoCE (%)	5.8	7.8	7.6	9.1	10.1
<b>Working capital &amp; liquidity ratios</b>					
Receivable (days)	29	26	30	30	30
Inventory (days)	33	29	40	40	40
Payable (days)	134	119	120	120	120
Current ratio (x)	0.9	0.8	0.9	0.8	0.8
<b>Valuation ratios</b>					
EV/sales (x)	4.6	4.1	3.8	3.5	3.2
EV/EBITDA (x)	22.5	20.9	18.2	16.2	14.1
P/E (x)*	156.3	55.0	47.2	36.8	31.3
P/BV (x)	3.8	3.6	3.4	3.1	2.8

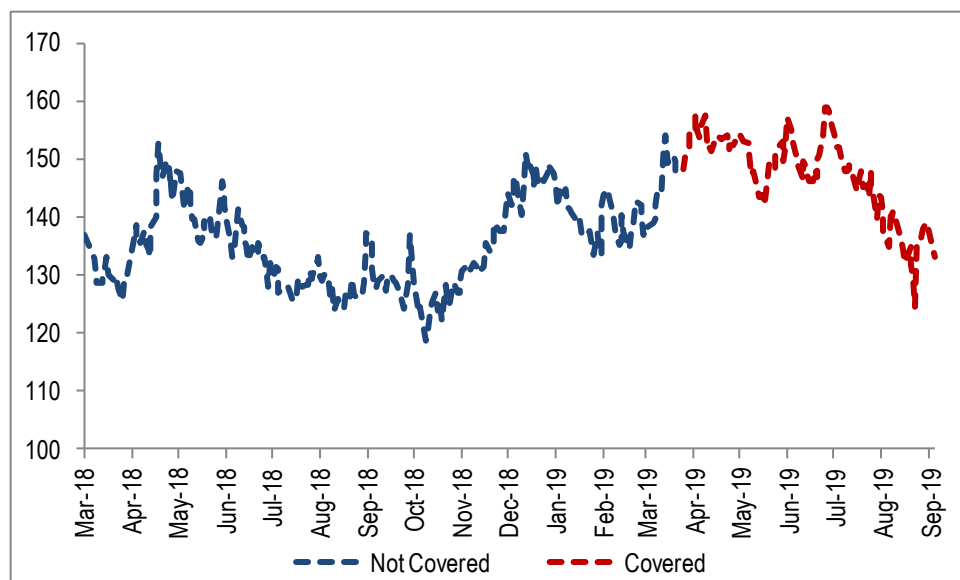
Source: Company, Nirmal Bang Institutional Equities Research

\*P/E is calculated on adjusted PAT

## Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
25 March 2019	Buy	148	195
8 April 2019	Buy	155	195
2 May 2019	Buy	154	195
5 July 2019	Buy	152	206
6 August 2019	Buy	135	206
5 September 2019	Buy	133	168

## Rating track graph



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ACCUMULATE -5% to 15%

SELL < -5%

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